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BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Statutory Review of the System	)	
for Regulating Rates and Classes	)	Docket No. RM2017-3
for Market Dominant Products	)	

VALPAK DIRECT MARKETING SYSTEMS, INC. AND THE VALPAK FRANCHISE ASSOCIATION, INC. INITIAL COMMENTS ON THE NOTICE OF PROPOSED RULEMAKING FOR THE SYSTEM FOR REGULATING RATES AND CLASSES FOR MARKET DOMINANT PRODUCTS
(March 1, 2018)

On December 1, 2017, the Postal Regulatory Commission ("Commission") completed its review of the ratemaking system as required by 39 U.S.C. § 3622(d)(3), 10 years after the enactment of the Postal Accountability and Enhancement Act ("PAEA"). *See* Order No. 4257, Order on the Findings and Determination of the 39 U.S.C. 3622 Review (Dec. 1, 2017) ("10-Year Report"). Also on December 1, 2017, the Commission issued Order No. 4258, "Notice of Proposed Rulemaking for the System for Regulating Rates and Classes for Market Dominant Products," seeking Initial Comments by March 1, 2018, and Reply Comments by March 30, 2018. Valpak Direct Marketing Systems, Inc. and The Valpak Franchise Association, Inc. (hereinafter "Valpak") hereby submit these joint Initial Comments on the proposed rulemaking.

I. The Commission's Proposal Offers One Important Way to Achieve the Objectives of the PAEA.

The Commission presents a comprehensive approach to reforming the ratemaking system for market dominant products. It requests from mailers and others "sound criticism of, concurrence with, or alternatives to the Commission's proposed approach." Order No. 4258 at 3.

The task before the Commission is of great importance to the nation. The provision in PAEA which delegates to the Commission the authority to conduct a review of the market dominant ratemaking system, and to make changes based on the findings of that review, is extraordinary. 39 U.S.C. § 3622(d)(3). Some commenters have viewed this grant of power to be a violation of the anti-delegation doctrine, as well as the Presentment Clause of the Constitution. Other commenters have taken the position that the Commission may not modify the price cap, or at least not substantially modify it. Laying aside for now the merits of those constitutional and statutory issues, this statute certainly entrusts to the Commission the responsibility to balance the competing interests of various postal stakeholders and develop a system that would serve all well into the future.

However, the type of system that will be devised by the Commission, no doubt with some later input from the U.S. Court of Appeals for the D.C. Circuit as well, necessarily must choose between two alternate, regulatory models. The first model was the "cost of service" model under the Postal Reorganization Act, which allowed the Postal Service to recoup all its costs, but entrusted pricing decisions to the Commission, withholding from the Postal Service the power to set its own prices to avoid the risk of it succumbing to the temptation of abusing market power over market dominant products. On the other hand, PAEA was designed to give a measure of pricing flexibility to the Postal Service — greater in the area of competitive products, but not inconsiderable with respect to market dominant products — while diminishing the pricing responsibility of the Commission, except to correct illegal pricing.

The differences between these two types of systems was highlighted by Commissioner Tony Hammond in his dissenting views to the Commission's proposal, which summarized the problem as follows:

> the changes proposed in this Order essentially constitute a return to the PRA's cost-of-service rates, but without any of the protection of the PRA framework. [Order No. 4258, Dissenting Views of Commissioner Tony Hammond at 1.]

Commissioner Hammond makes an important point. Whatever changes are made by the Commission, they must be designed to protect the mailers using market dominant products from arbitrary pricing decisions. PAEA built protections of mailers into the current system because a government monopoly has real market power over its customers. To the extent that the Commission's new pricing scheme is designed to allow recovery of all postal costs, it would have the effect of insulating the Postal Service from the consequences of its business decisions (and even declining productivity). Therefore, the Commission also must find new ways to ensure that mailers are protected in the process.

This need to protect mailers arises in numerous contexts. Among the most visible manifestations of this problem is existing pricing of Periodicals and Marketing Mail Flats, which together lose over $1.2 billion annually, and which drive up the prices for other mailers to cover those shortfalls. The Commission proposal incorporates many such protections of mailers, and it is urged that those provisions be included in the final pricing scheme, and even strengthened, as discussed herein.

II. The Proposed Rules Relating to Non-compensatory Products Are a Step in the Right Direction.

The Commission proposes special pricing rules for non-compensatory products and classes based on the 10-Year Report's conclusion that "non-compensatory products threaten the financial integrity of the Postal Service because the revenue from these products does not cover their attributable costs." Order No. 4268 at 73. That report concluded that rates for market dominant mail will meet the statutory requirement that they be "reasonable" only when "each class, and each product cover their attributable costs and are able to make a sufficient positive contribution to institutional costs." Order No. 4267 at 235. Accordingly, the Commission proposes to require the Postal Service (i) to increase the price cap by an additional 2 percentage points for non-compensatory classes, while requiring the Postal Service to apply all available pricing authority, and (ii) to increase prices for non-compensatory products within a profitable class by 2 percentage points above the average increase (with no additional increase of the price cap for that class). *See* proposed rules 3010.201 and 3010.202.

These commenters are encouraged by the Commission's recognition of the challenge to the financial stability of the Postal Service that underwater products have presented during PAEA. To remedy that growing problem, Valpak has urged the Commission to use its remedial powers to direct the Postal Service to achieve compliance with provisions of PAEA in many prior annual compliance reviews.[1]

The Commission's proposal to resolve non-compensatory products within a profitable class by directing price increases of at least 2 percentage points above the available pricing

[1] *See, e.g.,* Valpak Reply Comments, Docket No. ACR2017 (Feb. 12, 2018).

authority is an important step forward. This proposal should begin to increase the cost coverage of perennially underwater products, such as Marketing Mail Flats. However, it needs to be strengthened.

In the years since the Commission issued its remedial order for Marketing Mail Flats in the FY 2010 Annual Compliance Determination ("ACD"), the Postal Service has implemented only minimal price increases for Flats in all generally applicable rate adjustments, save one. The Commission's FY 2010 ACD order required the Postal Service increase the cost coverage of Flats to above breakeven through a combination of cost savings and price adjustments. FY 2010 ACD at 106. Despite the Postal Service's diligent efforts, meaningful cost savings were unable to be achieved, and the Postal Service's increases in Marketing Mail Flats' prices (5 percent — not percentage points — above the price cap, *i.e.*, CPI x 1.05) were modest, failing to even keep up with cost increases. *See*, *e.g.*, FY 2017 ACR at 15. And cost coverage of Flats has declined — now falling to 73.9 percent for the lowest cost coverage — according to the Postal Service's FY 2017 ACR. *Id.* at 13.

To be sure, the Commission's new proposal would require the Postal Service to increase prices for non-compensatory products such as Market Mail Flats by 2 percentage points above the available pricing authority. And this is a significant improvement over the Postal Service's interpretation of the Commission's remedial order issued in FY 2010 ACD. However, the Commission's analysis must be updated to include FY 2017 data.

In its proposal, the Commission presented two tables demonstrating how different scenarios could improve cost coverage for Marketing Mail Flats. Tables III-3 and III-4 showed cost coverage increases for three alternative above-cap pricing scenarios. Table III-3 assumes unit costs increase at 2.6 percent per year (assumed to be the annual rate of increase over the past eight years[2]), while Table III-4 assumes (without any historical justification) an increase of unit attributable costs at only 1.0 percent per year. *See* Order No. 4258 at 78-80. Table III-4's excessively optimistic assumption of unit cost increases allows it to show that the Commission proposal could cause Marketing Mail Flats' cost coverage to exceed 100 percent in five years. However, even Table III-3 is unduly optimistic.

Closer examination of cost trends demonstrates that costs are increasing faster than thought in the Commission's projected scenarios, and Flats are losing more money than had been thought. The Commission employed in its analysis the cost coverage of 79.4 percent reported by the Postal Service for FY 2016, the most recent year it had available for the 10-year review. The Postal Service filed the FY 2017 ACR about a month after Order No. 4258 was issued, showing that Flats' cost coverage had declined dramatically to 73.9 percent. Moreover, the Postal Service reported that Flats' unit costs increased nearly 10 percent in just one year. When the Commission's coverage analysis updates its starting point to use FY 2017 data, the charts presented change and become much bleaker:

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[2] This apparently is based on the total change in unit costs between FY 2016 and FY 2008, divided by 8.

Table I
USPS Marketing Mail Flats Cost Coverage Scenarios

	1.0%		2.0%		3.0%		4.0%	
Year	Coverage	Increase	Coverage	Increase	Coverage	Increase	Coverage	Increase
Year 0	71.4%	0.0%	71.4%	0.0%	71.4%	0.0%	71.4%	0.0%
Year 1	72.6%	5.05%	73.3%	6.05%	74.0%	7.05%	74.6%	8.05%
Year 2	73.7%	5.05%	75.1%	6.05%	76.6%	7.05%	78.0%	8.05%
Year 3	74.9%	5.05%	77.1%	6.05%	79.3%	7.05%	81.5%	8.05%
Year 4	76.1%	5.05%	79.1%	6.05%	82.1%	7.05%	85.2%	8.05%
Year 5	77.3%	5.05%	81.1%	6.05%	85.0%	7.05%	89.0%	8.05%
Total		27.93%		34.14%		40.58%		47.27%

Table I, *supra*, is essentially the Commission's Table III-3 (Order No. 4258 at 79) updated using unit costs and unit revenues as reported by the Postal Service in the FY 2017 ACR.[3] (It also adds a column for a 4.0 percentage points above average price increase scenario.) As can be seen, the percentage increase selected to be used in the Commission's proposed rule (2.0 percentage points) results in cost coverage at Year 5 that is fully 10 percentage points lower than the Commission's projection based on FY 2016 information (91.2 percent versus 81.1 percent). Even another percentage point increase does not help Flats achieve the level the Commission hoped for in Order No. 4258.

Moreover, what occurred during FY 2017 is more reflective of the cost trends of Marketing Mail Flats because FY 2016 was an outlier, as that year was more skewed by the FSS volume shifts. *See* FY 2016 ACD at 55. The FSS volume shifted back to Carrier Route in the first half of FY 2017, and that shift resulted in further deteriorated financial condition of

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[3] Year 0 does not account for the price adjustment that went into effect on January 21, 2018, just as the Commission's table did not account for the January 2017 price adjustment.

that product. *See* FY 2017 ACR at 15. Additionally, FY 2018 can be expected to be continue the trend in high cost increases for Flats and downward decline in coverage as it will be an entire year without the lower cost FSS Carrier Route pieces being included.

To achieve the Commission's five-year goal of 91 percent, the additional 2.0 percentage point increase proposed would need to be raised to at least 4.0 percentage points even if coupled with significant cost cutting strategies. *See* Table I, *supra*. Valpak urges the Commission to adopt a rule that will require the Postal Service to price non-compensatory products actually to achieve 100 percent cost coverage within a specified timeframe, such as five or six years. This approach would be consistent with objectives 1 and 8, as well as the objectives 2, 5, and 6.

III. The Productivity and Service Performance Based Pricing Authority Balances Financial Stability with the Need to Encourage Efficiency.

The Commission proposes to give two types of additional rate authority to the Postal Service. First, it grants an additional 2.0 percentage points of supplemental rate authority per calendar year for five full calendar years. This authority is said to be designed to provide medium-term financial security. In addition, the Commission proposes to grant up to an additional 1 percentage point of rate authority per calendar year — 0.75 percentage points based on operational efficiency tests, and 0.25 percent based on service quality-based tests. This additional authority is said to provide for long-term financial stability.

Applying these two new types of authority to a real world scenario, consider the last price increase, which was based on a CPI of about 2.0 percent. If the Postal Service qualified for both operational efficiency and service quality, the Postal Service would be able to raise prices by 5.0 percent for each class or product that was not underwater, for five years.[4]

Even putting aside the 1.00 percent that may be earned for operational efficiency and service quality, the proposed rules would permit a 4.0 percent price increase annually — and those annual increases would not all be based on some fixed initial base year, but would compound as the base increases.

It is axiomatic that the true measure of the success of a business is not its revenue growth, but rather productivity increases. Increasing productivity is necessary for the economic survival of a business:

> The level of productivity is the most fundamental and crucial determinant of a standard of living. Increased productivity allows people to get what they want faster, or to get more of what they want in the same amount of time. Supply rises with productivity, dropping real prices and increasing real wages; it lifts people out of poverty and allows them to focus on efforts beyond mere survival.... An increase in physical productivity causes a corresponding increase in the value of labor, which raises wages. [S. Ross, "Why is productivity an important concept in economics," Investopedia.]

A company that is suffering productivity declines has flaws that a system-wide price increase will only cover over for a time — but not solve. The Postal Service's Annual Report for FY 2017 revealed that Total Factor Productivity ("TFP") declined for the second year in a row, from 27.9 in 2015 to 27.5 in 2016 and to 26.8 in 2017.

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[4] Of course, for underwater classes and products, the increase could be greater, but that is not to be feared. Even if volume is lost by increasing rates on an underwater class or product, that benefits the Postal Service. No private company would offer large product lines which are priced below cost over the long term, and no governmental entity which is charged with the responsibility to be run in a business like manner could offer such products. Nevertheless, this is what is happening.

> TFP … decreased slightly in FY2017. This decrease was largely attributable to a decline in mail volume, increased transportation expenses and increased investments. A number of factors, including the decline in mail volume in recent years, has made it more challenging to generate additional productivity growth. [USPS FY 2017 Annual Report to Congress at 26.]

The Postal Service has sought to shift attention to another productivity-type measure, Deliveries Per Total Work Hour ("DPTWH"). The Postal Service explains that it uses "DPTWH rather than TFP as our primary indicator for two reasons: 1) DPTWH is easier to understand and target at the area and district level and 2) DPTWH can be calculated in a more timely manner than TFP, allowing us to more quickly assess our performance." *Id.* at 26, n.6. Unfortunately, even this measure declined in FY 2015 and again in FY 2017, so that from FY 2014 to FY 2017 it declined from 42.0 to 40.7 deliveries per total work hour (adjusted). *Id.* at 25. No explanation for these declines in productivity have been identified, other than that quoted above.

The Commission correctly identified the task at hand: "how to authorize the proposed supplemental rate authority in a manner that will put the Postal Service on the path to generating sufficient revenue to meet its medium-term obligations balancing all of the PAEA's objectives." Order No. 2458 at 41. However, granting the Postal Service additional revenue without any concomitant obligation to operate efficiently cannot be expected to put the Postal Service onto the correct path. Indeed, providing guaranteed revenue could operate as a disincentive to achieving necessary productivity increases. If the current incentives to increase productivity are inadequate to achieve that goal, this 10-year review rulemaking requires that changes must be made now. In the private sector, companies need to achieve increasing productivity in order to survive — even holding one's own is not a long-term model for success. In the government sector, if the Postal Service is rewarded financially while its productivity decreases, it will be given all the wrong signals, and could lead to even bigger problems, that could only be solved by a taxpayer bailout that no one wants.

Unless we are to return to cost-of-service ratemaking, with pricing set by the Commission, it is essential that there be meaningful incentives for the Postal Service to reduce costs and be more efficient. In recent years, it is apparent that incentives have not been sufficient to generate increases in productivity. For these reasons, it is suggested that the Postal Service not be given an automatic 2 percent increase for five years. Rather, if there is to be some increase, that it all be performance-based to provide a greater incentive, and grant the Postal Service additional CPI authority which is directly proportional to productivity increases. Thus, if productivity stagnates or even decreases, there would be no additional CPI authority.

IV. The Commission Should Not Implement the Proposed Five-Year Supplemental Pricing Authority but Should Consider Alternatives Instead.

Commissioner Hammond dissented from the proposed rules because they "elevate the financial stability objective above the others." Hammond Dissent at 1. Indeed, this statement appears correct from the face of Order No. 4258 with respect to the 2 percentage points supplemental pricing authority: "This proposed supplemental rate authority is necessary to achieve Objective 5." Order No. 4258 at 38. There does not appear to be any balancing of Objective 5 against the other eight objectives.

In the 10-Year Report, the Commission determined that it was the annual net losses in every year under PAEA that led to its finding that the Postal Service did not have medium-term financial stability, a function of Objective 5. *See* Order No. 4257 at 165-169. However, as noted by earlier ANM *et al*. Comments at 3-4, 23-25, 32-33, those stated financial losses obscure the operational profit that the Postal Service has earned for several years. Those stated losses are a function of other costs that are being accounted for by the Postal Service, such as the Retiree Health Benefits Fund payments, but which are not being made. If the Commission allows the price cap to be increased to make up for those unpaid expenses, will the Commission require that the revenue be used to cover those financial obligations going forward? If the funds are spent for other purposes, such as capital acquisitions (*see* Order No. 4258 at 47), the annual obligations will continue to be left unpaid. The reason the pricing authority is granted its use must correlate to the purposes for which the funds will be spent.

The 10-Year Report identified non-compensatory products as violating Objective 8's requirement for reasonable rate schedule, and jeopardized the financial integrity of the Postal Service, Objective 5. Order No. 4257 at 226. Below is Table II-15 from Order No. 4257 (at 234) showing the losses from all market dominant non-compensatory products under PAEA. More losses were added in FY 2017.

Table II-15
Non-Compensatory Products
Total Contribution (Loss) per Year (in $ Millions)

Product/ Fiscal Year	2008	2009	2010	2011	2012	2013	2014	2015	2016
First-Class Mail Parcels	-	-	-	-	(10)	(3)	-	-	-
Inbound Single-Piece Intl Mail	(102)	(105)	(53)	(33)	(93)	(95)	(54)	(75)	(28)
Standard Mail Flats	(227)	(616)	(577)	(643)	(528)	(376)	(411)	(520)	(604)
Standard Mail Parcels	(166)	(205)	(172)	(112)	(49)	(35)	(31)	(24)	(29)
Periodicals Within County	(4)	(13)	(24)	(19)	(28)	(21)	(18)	(22)	(25)
Periodicals Outside County	(434)	(629)	(587)	(590)	(642)	(500)	(490)	(490)	(505)
Bound Printed Matter Parcels	-	(7)	(27)	(4)	-	-	-	-	-
Package Services Media/ Library Mail	(60)	(74)	(89)	(98)	(56)	(56)	(20)	(85)	(88)
Package Services Parcel Post	(66)	(61)	(134)	(86)	(66)	(23)	-	-	-
Total Contribution	**(1,059)**	**(1,710)**	**(1,663)**	**(1,587)**	**(1,471)**	**(1,108)**	**(1,024)**	**(1,216)**	**(1,281)**

Source: Library Reference PRC-LR-RM2017-3/1

Valpak continues to point out that noncompensatory products require ongoing subsidies flowing from mailers of profitable products to mailers of those underwater products. Eventually, Valpak has argued, it would result in a system-wide price adjustment necessitated by the financial difficulties of the underwater products, imposing an actual price increase on all mailers to foot the bill. *See* Docket No. ACR2013, Valpak Initial Comment at 8, 48; Docket No. ACR2014, Valpak Initial Comments at 3, 10; Docket No. ACR2015, Valpak Initial Comments at 27-28.

The proposal to increase rates for all mailers because of Objective 5 is not balanced with Objective 8 for a "just and reasonable schedule," when the prices for all mailers are being increased because of the threat to the Postal Service's financial integrity caused by non-compensatory products. Accordingly, the Commission should focus any additional pricing authority on non-compensatory products, not an across-the-board 2 percentage point supplemental pricing increase on products that did not cause the problem.

V. The Commission's Ratemaking System Should Balance the Objectives to Protect High Cost Coverage Products.

Whether the price cap is limited to CPI as at present, or if the cap includes supplemental pricing authority, the Postal Service will continue to have considerable pricing flexibility (Objective 4). But just as financial stability (Objective 5) should not take precedence over all the other objectives,[5] neither should pricing flexibility. It must be balanced with the other objectives, including achieving "a just and reasonable schedule for rates" (Objective 8), and establishing "incentives to reduce costs and increase efficiency" (Objective 1) (*see also* Factor 7). Furthermore, the ratemaking system must take into account PAEA factors, including the requirement that each class or type of mail service, including each product,[6] bear its attributable costs (Factor 2), and the "effect of rate increases" (Factor 3).

Valpak urges the Commission to include in its new rate setting system a mechanism that limits above average price increases on products that already have high cost coverage especially when compared with other products within a class. Such a mechanism would not "prohibit the Postal Service from making changes of unequal magnitude within … classes of

[5] *See* Commissioner Hammond dissent at 1.

[6] *See* FY 2010 ACD at 17-18.

mail" (§ 3622(b)(8)), but it would ensure there would be effect given to the other objectives and factors to constrain price increases on already very high cost coverage products.

By way of illustration, Table II compares cost coverages of HD/Saturation Letters and HD/Saturation Flats & Parcels. Generally, the cost coverage of HD/Saturation Letters has remained high — well above 200 percent — while the cost coverage of HD/Saturation Flats & Parcels has been declining to a level near the systemwide average. In FY 2008, the coverage of HD/Saturation Flats & Parcels exceeded HD/Saturation Letters by 26.4 percentage points. Now, as of FY 2017, the relationship has reversed, and HD/Saturation Letters are required to pay prices reflecting a 54.4 percentage point higher coverage than HD/Saturation Flats & Parcels. *See* Table II.

Table II
Marketing Mail Saturation Products
Cost Coverages
(FY 2008 – FY 2017)

	HD/Sat Letters	HD/Sat Flats & Parcels
2008	230.8%	257.2%
2009	216.0%	239.6%
2010	212.8%	224.4%
2011	221.2%	213.6%
2012	222.2%	217.3%
2013	235.8%	229.0%
2014	238.0%	227.6%
2015	218.5%	173.3%
2016	218.4%	168.4%
2017	211.5%	157.1%

Without any clear reason, over the period of PAEA, the coverage for HD/Saturation Flats & Parcels has dropped by 100 percentage points while HD/Saturation Letters continue to pay more than double its costs.

Some of the reason for this reversal in coverage could be the result of cost changes. For example, unit costs of HD/Saturation Flats & Parcels increased at three times the rate of increase of HD/Saturation Letters over the past four years. *See* Table III.

Table III
Marketing Mail Saturation Products
Unit Costs (FY 2012-FY 2017)
(cents)

	FY 2012 Unit Costs	FY 2017 Unit Costs	FY 2012-2016 Change	Percentage Change
HD/Sat Letters	6.24	7.26	1.02	16.3%
HD/Sat Flats & Parcels	7.65	11.22	3.57	46.7%

However, rather than being rewarded for improved mail makeup that allows its mail to be handled at increasingly low cost, HD/Saturation Letters mailers appear to have been penalized for that efficiency — by being charged an exorbitant coverage. This result is unjust[7] and unreasonable. It also sends the wrong price signals to mailers to enter more mail as flats that the Postal Service cannot handle as efficiently, and fewer letters. All Marketing Mail is advertising, and there should be clear justification for dramatic intraclass cost coverage disparities, but today there is none.

[7] Valpak respectfully disagrees with the Commission's finding in the 10-Year Report that the prices have been "just" under PAEA. *See* Order No. 4257 at 130.

Another way to view the disparity of cost coverages within Marketing Mail would be to compare Marketing Mail Flats with HD/Saturation Letters. In FY 2017, the difference between the coverages for Flats and HD/Saturation Letters was 137.6 percent. Here too, the disparate treatment of similar products that all consist of advertising within one class is unexplainable, especially between the Flats product that loses hundreds of millions of dollars annually ($669 million), while the HD/Saturation Letters product that generates hundreds of millions of dollars annually ($574 million). In the private sector, businesses do not penalize their best customers, and force profitable customers to subsidize those customers who purchase unprofitable products.

The cost coverage of letter-shaped products remains high (Marketing Mail Letters has been hovering around 200 percent cost coverage; HD/Saturation Letters is always over 200 percent cost coverage) as the unit cost of those pieces has been relatively stable. Meanwhile, the coverages of non-letter-shaped products have been declining, as their costs have been increasing.

Any pricing system that includes "transparency of the ratemaking process" (Objective 6) should also encourage operational efficiency (Objective 1, Factor 7). Neither the current system nor the proposed system does that, but the proposed system could be easily modified to ensure these important statutory objectives and factors are not ignored in pricing decisions to protect mailers of high coverage products.

VI. The Proposed Rules on Workshare Discounts Provide for Greater Pricing Flexibility for the Postal Service and Encourage More Efficient Operations.

The Commission's Order contains a thoughtful analysis of workshare discounts. It generally embraces the concept of Efficient Component Pricing within a system that leaves some flexibility to adjust to changing cost estimates.

However, for a variety of reasons, certain workshare discounts for SCF-entered Marketing Mail (*e.g.*, HD/Saturation Letters, SCF entered) currently exceed the proposed workshare pricing band of between 80 and 115 percent (at 147.6 percent). In Docket No. ACR2017, the Postal Service explained this problem as follows:

> In Docket Nos. ACR 2016 and R2018-1, the Commission accepted the Postal Service's reliance on 39 U.S.C. § 3622(e)(2)(B) to justify these passthroughs, contingent on the Postal Service's adherence to a plan to reduce passthroughs by 10 percentage points in each market dominant rate case. The Postal Service continues to justify these passthroughs pursuant to 39 U.S.C. § 3622(e)(2)(B); it plans to recommend to the Governors reduction in the passthroughs of at least 10 percentage points in the next market dominant rate case, subject to adequate pricing flexibility, operational efficiencies, and changes in cost avoidance. [FY 2017 ACR at 22-23.]

As the Postal Service has begun this process to reduce the passthroughs over a period of time, Valpak would urge the Commission to continue to allow that process to continue in this measured manner. In the alternative, Valpak would urge the Commission to adopt the wider band being used for Periodicals, from 75 percent to 125 percent, so as to minimize the rate shock from any more rapid change in passthroughs for SCF-entered letters.

Further, it should be understood that passthroughs as currently measured do not reflect many of the costs avoided by efficient makeup of this highly efficient workshared mail. This issue has been recognized and discussed for some time.[8]

Lastly, it must be recognized that the cost coverage paid by HD/Saturation Letters are the highest in Marketing Mail, and among the highest in the entire Postal Service — 211.5 percent. Clearly, it would be profoundly unfair to subject the most efficient of these letters, those entered at a destination SCF, to an additional price increase at this time.

Respectfully submitted,

/s/

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[8] *See* Dr. John Haldi & William J. Olson, "An Evaluation of U.S. Postal Service Worksharing: Postal Revenues and Costs from Workshared Activities," Competitive Transformation of the Postal and Delivery Sector, (Eleventh Conference on Postal and Delivery Economics Rutgers University Center for Research in Regulated Industries, Toledo, Spain, June 4-7, 2003).